A Synopsis On

An Empirical Analysis of Performance of Indian Banking (Under CAMEL Model Approach)

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Supervisor -
Dr. Manish Didwania

Submitted by
Krishna Murari 27.10.09

Department of Commerce
Faculty of Arts, Science & Commerce
Mody Institute of Technology & Science
(Deemed University)
Lakshmangarh

INTRODUCTION

As India has witnessed as one of the fastest growing economies in world (second to china) one sector, which has played a vital role in propping up its economy, is undoubtedly the banking sector. The financial reform process and resulting liberalization that started in year 1991 have put the banking sector in an atmosphere, which was never before. Interest rates were deregulated and prudential norms were introduced. The entry of new players like the new private & foreign banks with their state of art technology and improved customer services made the competition in the banking sector more keen and intense.

During the past six decades, since independence the banking sector has seen the significant changes in the banking arena in the country with technology being a major facilitator of this transformation. ATMs, Internet banking, credit cards and now mobile banking have helped to revolutionize the banking scenario n the country. With the use of their newfound tech-savvy and increased thrust on product/services innovation, the Indian banking has contributed a lot toward a phenomenal growth of economy (India's GDP grew in excess of 8% consistently since 2003-04 onwards with a growth of 9% to 9.2% in 2005-06 and 2006-07 respectively). In last couple of years, the banking sector has reported a sterling performance. According

to economic survey 2006-07, the Scheduled commercial banks (SCBs) showed a sharp rise in their total income during 2005-06, growing by 16.8% as against 3.5% in 2004-05. Interest income also grew sharply by 18.4% in 2005-06 as against 7.9% in previous year. The operating profit of the banking sector (including SBI & its associates, nationalized banks, private sector banks & foreign banks) has also gained momentum. A similar trend has been observed on the basis of other performance barometer of banking.

The CAMEL model is considered as the performance barometer of banking sector, which includes 5 major parameters i.e. Capital adequacy, Asset quality, Management, Earnings and Liquidity position. The empirical study based on above parameters will also provide an insight into how the Indian banking industry is capable to face the challenges ahead. One of the biggest challenges facing the Indian banking is making a smooth transition to a tougher regime i.e. Basel II. Further as more and more domestic banks aspire to have global presence, they would not only need a scale but also a robust risk management system. Taking in to account such types of challenges ahead, we shall also be focusing on the future prospects of the Indian banking.

Here in this proposed research work an attempt will be made to analyze the bank's performance using the renowned CAMEL model for the

recent 5 years. The present study is conducted for three major sectors of Indian banking i.e. Public sector banks, Private sector banks and Foreign banks.

Objective of the study

As any research work without objective is just like a journey with no destination. Therefore the objectives of the study are-

- To obtain a true insight of the performance of banking sector in India.
- To study the significant change that have taken place in Public sector, Private sector and Foreign banks in the last five years and to judge the efficiency on the basis of the CAMEL model approach.
- To have a glimpse on reforms, norms and guidelines issued by RBI to maintain the pace of growth of Indian banking.
- Further we shall also focus on to the deeper insight to the challenges and prospects for Indian banking system.

Significance of the proposed research work

The present study will be an attempt to explore the analysis of the performance of Indian banking sector. For the sake of research work we have categorized the Indian banking in Public sector banks(PSBs), Private sector banks and Foreign banks. The significance of the proposed research work can be seen for the following users-

To the Management- The managers are responsible for current and long-term profit from operations and effective deployment of banks. An empirical analysis of performance of banks may bring an overall view of the effectiveness of its own policies & decisions.

To the Government- The Government regulates economic activities in various spheres and as such is closely interested in the health of the banking sector as a whole. To levy various taxes, granting aids, sanctioning financial assistance to the banks, Government also require the analysis of the performance of the banks.

To the Employees- The employees have an interest in operating and financial strength of the bank. The past operating performance as well as the current financial position is often studied to measure the ability of bank to meet its wages commitment.

To the Society & Others- Society as a whole also wants to know about the financial soundness of the banks for the sake of their transactions with a financially strong bank. The study may provide a broader perspective to help them in this regard.

Review of literature

A lot of literature is available on banks relating to their role in economic development of a country, problems faced by them, challenges before them

and strategies adopted to tackle them. But literature on empirical analysis of performance of PSBs, private sector banks and foreign banks under CAMEL model approach is scanty. Most of the literature available is in the form of individual study based on different parameters in their articles. Some worthwhile studies relating to the present topic are being reviewed here.

- In May 2007,Mr. Roji George, Dr. V Charles, Dr. (Mrs.) Kumudha A. presented a paper in conference on a topic entitled "A C.A.M.E.L. Model analysis of new Private Sector Banks in India". In this paper they focused on the newly formed private sector banks only. They did not touch the real contributing sector i.e. public sector banks. In their study they concluded that while considering all the years' performance, Kotak Mahindra Bank was the best bank followed by HDFC Bank and Indusland Bank. Year wise performance of banks revealed that, none of the new private sector banks were performing well. During 2004-05 Kotak Mahindra was placed as the best bank and in 2003-2004 it was HDFC Bank, Induslnd Bank and UTI Bank. It was found that except Centurian bank, all our banks had sound Capital Adequacy, the main concern of Basel norms.

- K. Prabhakar Rajkumar (2007) evaluated the earning performance of 28 private sector banks during 2005-06. He concluded that overall net profit had increased by 42% during 2005-06
- Reddy & Bhargavi (2004) appraised Indian banking from NPA perspective. They took NPA management in SBI and concluded that the gross NPA of SBI was more or less constant around 15% from 1997 to 2000. They also proposed guidelines for effective NPA management.
- D'souza (2002) in his study evaluated the performance of public sector, private sector and foreign banks on the basis of profitability. The analysis revealed that the profitability of the public sector banks in nineties improved relatively to that of private and foreign banks.
- Ram Mohan (2002) in his paper documented & evaluated the performance of public, private and foreign banks. He takes up the issues of trade off between efficiency & stability in banking.
- Subramany & Raghav (2001) compared efficiency in the six public sector banks, four private sector banks and three foreign banks. He analyzed that the Bank of Baroda from public sector and City bank from private sector registered the highest efficiency and operational profit per employee.

- Singh (2001) made an attempt to assess the impact of the reforms on the operational performance and efficiency of the commercial banks in India. It was observed that in the public sector banks, the size of the NPAs has reduced to some extent.

Collection of data

Basically the data for the study will be collected from secondary sources. The secondary sources shall be comprised of the publication of the banks, publication of RBI & CMIE and other research publications relevant to the study. Further the data will be collected from banks directly wherever necessary. The data will be collected for the recent period of 5 years i.e. for the five years back to the submission of thesis.

Although the entire analysis depends on secondary sources but necessary relevant study material will be collected from interviewing the banking experts and it will be an attempt to authenticate the study.

Method of study

For the purpose of analyzing the performance of Indian banking sector, a performance barometer i.e. CAMEL model will be used. The CAMEL model comprises of percentages and ratios for the interpretation and analysis of the study. In brief under CAMEL model approach following percentages and ratios will be used.

- **Capital adequacy** is considered as on of the key components of the CAMEL model to assess the financial health of a bank. Under capital adequacy the banks will be assessed with the help of the capital adequacy ratio (CAR), debt- equity ratio, advances to assets ratio G-securities to investment ratios.
- As the capability & strength of a bank lies in the quality of its assets, a comprehensive analysis of **asset quality** is vital to assess the current state of affairs and future viability of the bank. The efficiency of banks in assessing the credit risk and recovering debt is indicated by net NPA to total asset ratio, net NPA to net advances, total investment to total assets and % change in net NPAs.
- The **management** of bank ensures the development & endurance of a bank. The ratio of the total advances to deposits indicates the ability of a bank to effectively deploy its resources. Similarly profits per employee, business per employee and return on net worth (RONW) are very good productivity indicators.
- Profitability of the bank and also its ability to earn consistently can be easily determined by its **earning quality**. Thus % growth in net profit, spread, interest income to total income, non-interest income to total income are used to assess the earning quality of banks.

- Last but not the least is the **liquidity**, which is very crucial for any organization, which deals with money. It is more important for banks. Liquidity is compared primarily based on two parameters i.e. liquid assets to total deposits and liquid assets to total assets.

The techniques of ratio analysis, trend analysis and common size statement analysis will be used to draw conclusion. The processing, classification, tabulation and interpretation of data will be done as per the ease of the study.

Contribution to knowledge

The empirical analysis of the performance of Indian banking will make a significant contribution to knowledge. Further it will provide suggestion of practical significance to the public sector banks, private sector banks and foreign banks for advancement in future.

Hypothesis

The present study aims at testing a set of hypothesis with its findings. The following hypotheses are formulated keeping in view the objective of the study, method adopted to analyze the performance of banks and various internal & external factors.

- The Indian banking sector does not meet the minimum capital adequacy norms as prescribed by the RBI.

- Public sector banks, private sector banks & foreign banks do not have standard practices to maintain a sound quality of assets, which leads to increase in their NPA.
- The Indian banking sector does not have adequate and updated management policies to deploy the capital and meet the ever-increasing needs & wants of the customers.
- The banking sector has followed a wild-branch-expansion policy to increase the ability of a bank to earn consistently, which basically determines the profitability.
- The three major categories of banking sector are suffering with liquidity crisis.
- Indian banking sector is competent enough to meet the challenges for maintaining the asset quality, implementing the Basel II norms and for preparing a road map for banking in global context.

Limitations of the study

Since the study is mainly based on secondary data, so the quality of this research work is dependent on quality & reliability of data published in the reports. It is not possible for an independent researcher to question the validity & reliability of data published in reports. Therefore they are presumed to be reliable.

Finally this empirical analysis of 5 years is not a complete story of banking sector, but just a chip of old block. Still the period is confined to 5 years due to practical limitations. Thus the picture presented can show the trends, relative increment and decrement but not an absolute image.

AN OUTLINE OF THE PROPOSED RESEARCH WORK

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2.4 History of private sector banks

2.5 History of foreign banks

2.6 Role of 3 banking sectors to economic development

Chapter-3: Banking reforms in India

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3.2 Post independence to pre liberalization

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Chapter-4: The CAMEL model approach

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4.3 Asset Quality

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Chapter-6: Findings and interpretation

6.1 Emerging trends in banking sector

6.2 Challenges ahead for Indian banking

6.3 Future prospects

Chapter-7 Conclusion and suggestions

7.1 The changing paradigm of banking sector

7.2 Suggestions for improvement

7.3 Conclusion

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Dean
Faculty of Arts, Science & Commerce
Mody Institute of Technology & Science
(Deemed University)
Lakshmangarh, Sikar (Raj.)